



Signed and Filed: November 09, 2009

Dennis Montali

DENNIS MONTALI
U.S. Bankruptcy Judge

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF CALIFORNIA

In re) Bankruptcy Case
GEORGE QUINN CHEN,) No. 03-32157DM
Debtor.) Chapter 7
E. LYNN SCHOENMANN, as Trustee of) Adversary Proceeding
the Chapter 7 Estate of George) No. 07-3108DM
Quinn Chen, Debtor,)
Plaintiff,)
v.)
GEORGE QUINN CHEN, an individual,)
CYNTHIA WONG, an individual,)
SHANGHAI 1930 LLC, a California)
limited liability company, and)
SHANGHAI 1930 RESTAURANT PARTNERS,)
L.P., a California limited partner-)
ship,)
Defendants.)

MEMORANDUM DECISION ON COMPLAINT TO REVOKE
DISCHARGE AND TO RECOVER MONEY

I. INTRODUCTION.

E. Lynn Schoenmann, the Chapter 7¹ trustee ("Trustee"),

¹ Unless otherwise indicated, all chapter, section and rule references are to the Bankruptcy Code, 11 U.S.C. §§ 101-1532, and to the Federal Rules of Bankruptcy Procedure, Rules 1001-9037 in effect

1 initiated this adversary proceeding by filing a complaint (the
2 "Complaint") against George Q. Chen ("Debtor"), his wife, Cynthia
3 Wong ("Wong"), Shanghai 1930 LLC ("Shanghai LLC"), and Shanghai
4 1930 Restaurant Partners, L.P. ("Shanghai LP") on September 24,
5 2007. The Complaint sought declaratory relief regarding Debtor's
6 ownership interest in Shanghai LLC, the avoidance of postpetition
7 transfers and revocation of the Debtor's discharge.

8 More specifically, the Complaint sought a determination that
9 as of July 23, 2003, the date of commencement of this bankruptcy
10 case (the "Petition Date"), the Debtor was the sole member of
11 Shanghai LLC. The Debtor contended that as of the Petition Date,
12 Wong owned a 51% membership interest in Shanghai LLC, by way of
13 transfer from the Debtor. On this claim for relief the parties
14 brought cross motions for summary judgment and the Court granted
15 summary judgment in favor of the Trustee on November 14, 2008,
16 determining that all membership interests in Shanghai LLC were
17 owned by the Debtor as of the Petition Date.

18 On October 21, 2008, Shanghai LLC and Shanghai LP were
19 eliminated as defendants by way of their summary judgment motion
20 that was not opposed by the Trustee.

21 On April 20, 2009, the Debtor and Wong, the only remaining
22 defendants, filed a motion seeking reconsideration of the court's
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24
25 prior to October 17, 2005, the effective date of most of the
26 provisions of the Bankruptcy Abuse Prevention and Consumer
Protection Act of 2005, Pub. L. 109-8, April 20, 2005, 119 Stat. 23,
as Debtor's case was filed prior to its effective date.

1 ruling in favor of the Trustee on the first claim for relief. On
2 August 4, 2009, the court issued its Memorandum Decision on Motion
3 to Reconsider, stating its reasons for denying the motion. That
4 denial will be incorporated into the Final Judgment to be issued.

5 By the second claim for relief, the Trustee seeks to avoid
6 and recover numerous postpetition transfers made by Shanghai LP
7 (under the Debtor's and Wong's control and direction) to the
8 Debtor and Wong during the period between the Petition Date and
9 the date of sale of the estate's ownership interest in the
10 Restaurant (as hereafter defined) to Wong.

11 In the third claim for relief, the Trustee seeks revocation
12 of Debtor's discharge.

13 The matter was tried to the court on June 1 & 2, 2009;
14 appearances were noted in the record. Having considered the
15 testimony of the witnesses, the documentary evidence, and the
16 arguments of counsel, the court now issues its decision, subject to
17 further consideration of the evidence as discussed below.

18 For the reasons to be explained, on the second claim for
19 relief the court will award Trustee damages in the sum of
20 \$38,806.84 against Debtor based upon his receipt of that amount by
21 way of two equity distributions that were property of the estate
22 and in the sum of \$729,044.19 based upon proof that he received at
23 least that amount on account of a prepetition loan owed to him
24 that also was property of the estate. The court will award
25 Trustee damages in the sum of no less than \$11,000 against Wong
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1 based upon her receipt of a portion of the debt owed to Debtor.
2 It will not award damages against Wong based upon her receipt of
3 two equity distributions.

4 On the third claim for relief, Debtor's discharge will be
5 revoked.

6 II. FACTS.²

7 The Debtor filed for chapter 13 relief on July 25, 2003 (the
8 "Petition Date"). The Debtor's case was converted to chapter 11
9 on August 13, 2003, and Trustee was appointed. Then on July 15,
10 2005, the Debtor's case was converted to chapter 7; the Trustee
11 continues to serve as trustee. The court entered an order
12 discharging the Debtor on October 26, 2005.

13 Debtor founded a restaurant known as "Shanghai 1930" in 1997
14 in San Francisco, California (the "Restaurant"). It has operated
15 ever since, and is owned and operated by Shanghai LP, the general
16 partner of which is Shanghai LLC. Debtor was the 100% separate
17 property owner of Shanghai LLC. Debtor and Wong are also limited
18 partners in Shanghai LP.

19 On April 25, 2007, Debtor filed a motion seeking the estate's
20 abandonment of his interest in Shanghai LP. His expert appraisal
21 witness concluded that that interest had a nominal or no value as
22 of February 28, 2007.

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25 ² The following discussion constitutes the court's findings
26 of fact and conclusions of law. Fed. R. Bankr. P. 7052(a). Some of
the findings are based upon the parties' Stipulation Of The Parties
To Undisputed Facts filed May 29, 2009 (docket # 76).

1 In opposition the Trustee located a third-party buyer willing
2 to buy the estate's interest for \$25,000. Wong objected to the
3 sale and ultimately purchased the estate's interest for \$50,000.

4 With the approval of the court, Trustee sold all of the
5 estate's interests in Shanghai LP and Shanghai LLC to Wong on
6 November 14, 2007 (the "Sale Date"). The sale did not include any
7 claims held by the estate against the Debtor or Wong with respect
8 to payments made by either Shanghai LP or Shanghai LLC prior to
9 the Sale Date. At issue before the court are activities that
10 occurred between the Petition Date and the Sale Date (the "Subject
11 Period").

12 As of the Petition Date there was an outstanding amount owed
13 by Shanghai LP to the Debtor of no less than \$935,709.98 (the
14 "Chen Loan"). The Chen Loan is reflected in Shanghai's general
15 ledger as a liability account (Loan from George Chen - Account
16 2300, or "Chen Loan Account"). Most, if not all, of the Chen Loan
17 represents cash advances Debtor made prior to the Petition Date to
18 help the Restaurant deal with cash flow needs, including covering
19 employees' tips, cash purchases, etc. The Trustee was unaware of
20 the existence of or the outstanding balance on the Chen Loan until
21 conducting discovery involving the sale of the estate's interest
22 in Shanghai LP because the Debtor did not list it on his
23 schedules. The Trustee has received no payments from Shanghai or
24 anyone else on account of the Chen Loan.

25 A. Equity Distributions.
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1 During the Subject Period, and disregarding management fees
2 and salary payments, \$20,880 was paid to the Debtor in December,
3 2005 and \$17,926.84 more in April 2007. The same amounts were
4 paid to Wong on the same dates, and all four payments were
5 distributions on equity interests in Shanghai LP (the "Partner
6 Distributions"). The Partner Distributions to Debtor were
7 property of the estate, as the estate owns the entirety of
8 Shanghai LLC and Debtor's limited partnership interest in Shanghai
9 LP. Trustee did not prove that Wong's Partner Distributions were
10 on account of her own interest as a limited partner in Shanghai
11 LP.

12 Debtor attempts to justify his Partnership Distributions on
13 the basis of his apparent belief that Trustee told him after entry
14 of his discharge that he could build the Restaurant. The Trustee
15 did not authorize him to withdraw and keep any Partner
16 Distributions as Debtor never asked Trustee about them.

17 B. Payments on the Chen Loan.

18 Trustee contends that during the Subject Period the Debtor
19 and Wong caused Shanghai LP to repay the entire balance of the
20 Chen Loan to the Debtor and Wong, in the amount of \$935,709.98.
21 She maintains that Shanghai had sufficient cash to make those
22 payments from its cash sales to customers. Debtor contends that
23 these payments to him were on account of post-petition loans or
24 alternatively that the Restaurant lacked sufficient cash to make
25 any payments on the Chen Loan. He contends that the Restaurant's
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1 outside bookkeeper simply used the Chen Loan Account to post
2 transactions that were not otherwise documented, primarily cash
3 the Restaurant needed to pay weekly to its servers as tips that
4 were given by customers via credit card charges. The bookkeeper,
5 only a few weeks prior to trial, came to realize that cash used to
6 pay those tips to the servers should have been posted as such,
7 rather than shown as advances by Debtor, increasing the Chen Loan.
8 These were described at trial as "unsubstantiated entries."
9 Similarly, she maintains that reductions in the Chen Loan account
10 were not that at all, but were simply incorrect postings.

11 The Trustee's accounting expert prepared a report that
12 demonstrated that Debtor received transfers during the Subject
13 Period by checks to various payees, including the Debtor, Wong,
14 "cash," and "Shanghai 1930." Some of those payments were debited
15 to sales and sales tax accounts, resulting in a reduction of
16 reported sales.

17 If the journal entries that resulted in an increase to the
18 Chen Loan account actually reflected reimbursements to the Debtor,
19 such reimbursements would be posted as costs in the "costs of
20 sale" or "operating expenses" accounts.

21 Although the Chen Loan account balance increased during the
22 Subject Period, the increases were largely based on the
23 unsubstantiated entries made by the bookkeeper on the books.
24 Basically, because she was not aware of the Restaurant's recording
25 of tips, she increased the Chen Loan balance for any otherwise
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1 undocumented receipts. Actual restaurant sales were reported to
2 her on a reliable point-of-sale system; credit card receipts,
3 representing 95% of all Restaurant revenues, were greater than
4 reported sales because customers included sales taxes and tips;
5 sales taxes were easily calculated and paid by the bookkeeper, but
6 since she did not know about the tips, she assumed the additional
7 cash came from Debtor and posted it accordingly. In fact, five
8 percent of the Restaurant's sales revenues came from cash-paying
9 customers.

10 When she had more money on hand than was reported in sales of
11 the Restaurant, the bookkeeper automatically attributed that
12 excess to monies that came from Debtor by posting increases in
13 Account 2300, using it as a balancing account because of the lack
14 of credible documentation. However, the Debtor, Wong nor the
15 bookkeeper provided documents to substantiate such a practice.

16 Debtor's claims that he advanced monies to the Restaurant
17 post-petition, but he has offered no documentary evidence or
18 entries in the Restaurant's books and records to support that
19 contention. The evidence establishes that what the bookkeeper
20 posted as postpetition payments on the Chen Loan should have been
21 booked as expenses. Further, Trustee's expert examined the
22 records and concluded, convincingly, that Debtor did not make any
23 significant advances to increase the Chen Loan. They cannot be
24 verified through corresponding bank deposits.

25 The court is faced with the task of determining whether there
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1 were in fact payments to Debtor and/or Wong on the Chen Loan
2 during the Subject Period. On the Trustee's side there is an
3 expert report (Exhibit 14), modified by and adjusted after
4 accepting the bookkeeper's concessions of erroneous postings of
5 unsubstantiated transactions and cash payments (Exhibit 19); on
6 the Debtor's side there is no expert witness, inconclusive and
7 somewhat confusing financial accounting, and capable counsel's
8 creative arguments and speculation about large amounts of unproven
9 tip receipts that do not amount to evidence. On balance, the
10 preponderance of the evidence supports the court's acceptance of
11 the Trustee's accountant's opinion that at least \$729,044.19 of
12 the Chen Loan was paid to Chen or Wong during the Subject Period.
13 The court rejects the Trustee's suggestion that under a last-in,
14 first out theory, Chen should be liable for the entire amount of
15 the prepetition Chen Loan, \$935,709.98.

16 At the minimum, Chen is liable to the estate in this amount
17 of repayments of the Chen Loan. As to Wong, the specific
18 evidence alluded to by Trustee's counsel during argument is found
19 in Exhibit 1, p. 1147. There the court notes a total of \$11,000
20 paid to Wong and booked as payments on the Chen Loan. As such,
21 Wong had no right to that money, has not proven that she was
22 otherwise entitled to it, and must reimburse the estate for it.

23 Whether Wong received more than \$11,000 on the Chen Loan may
24 have been established in the documentary evidence, but the court
25 will not wade through that detailed evidence to find other similar
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1 entries to make out the case against Wong. But to the extent the
2 admitted evidence does show similar disbursements, the court will
3 permit the Trustee to point out such disbursements and add them to
4 the amount of Wong's liability, as discussed in the Conclusion to
5 this Memorandum Decision.

6 Postpetition, the Debtor claims that he has had an ongoing
7 relationship with the Restaurant whereby he purchases wine,
8 restaurant supplies and other merchandise and is reimbursed for
9 it. These "reimbursements" are reflected on the Restaurant's
10 books and records as payments on the Chen Loan. There is no
11 indication to which debt the payment is applied. Accordingly,
12 when payment is made on an obligation, unless there is some
13 indication to the contrary, the practical and ordinary
14 interpretation must "undoubtedly be that payment is to be applied
15 to the part first coming due to be paid." Smith v. Renz, 122 Cal.
16 App. 2d 535, 538 (Cal. App. 1st Dist. 1954).

17 The Petition Date balance of the Chen Loan of \$935,709.98 is
18 an earlier obligation than any postpetition advances, and
19 therefore any pay-down of the Chen Loan must be credited to the
20 prepetition debt. No logical reason has been offered as to why, in
21 the ordinary course of events, it should be approached in inverse
22 order. Therefore, it must be assumed that if the parties intended
23 to "depart from the ordinary" they would have specifically so
24 provided. Id.

1 Because general credits on open accounts stand as payments on
2 the oldest items of such accounts, the Debtor's contention that
3 the payments made were post-petition reimbursements for post-
4 petition advances is incorrect. Jessup Farms v. Baldwin, 33 Cal.
5 3d 639, 190 (Cal. 1983).

6 The Trustee's counsel asked that all of the amounts repaid
7 Chen Loan during the Subject Period be declared as a joint and
8 several liability of Chen and Wong. Absent facts and law to
9 support such a result, the court will not do that. Wong's
10 liability is limited to distributions to her on the Chen Loan.

11 C. Revocation of Discharge.

12 The Debtor was aware of the Chen Loan when he filed his
13 bankruptcy petition, related schedules and statement of financial
14 affairs, but he failed to disclose this substantial debt owed to
15 him. His Schedule B declared no debt owing. It showed
16 \$228,141.17 in personal property, \$200,000 of which was stock in
17 an unrelated company that has since been sold. Debtor also knew
18 that payments on the Chen Loan and the Partnership Distributions
19 made during the Subject Period belonged to the estate, but he
20 knowingly failed to report them or turn them over to the Trustee.

21 Debtor also misled the Trustee when he argued that the
22 estate's interest in Shanghai LLP had a nominal value at best and
23 the Restaurant was operating at a loss when in the same year he
24 and received a Partnership Distribution of \$17,926.,84, having
25 earlier received a Partnership Distribution of \$20,880.

1 Property of the estate includes money that a debtor has a
2 right to receive. In re Crysen/Montenay Energy Co., 902 F.2d
3 1098, 1101 (2d Cir. 1990) (debtor's right to collect accounts
4 receivable is "property of the estate"). An outstanding loan that
5 a debtor expects to be repaid is property of the debtor's
6 bankruptcy estate. In re Martin, 141 B.R. 986, 993 (Bankr. N. D.
7 Ill. 1992). The Chen Loan and the right to collect it became
8 property of the Estate as of the Petition Date. All payments made
9 on account of that loan prior to the Sale Date, therefore,
10 belonged to the estate. Debtor and Wong had no right to retain
11 the payments on the Chen Loan that they received.

12 Similarly, the two Partner Distributions to Chen made prior
13 to the Sale Date constituted property of the estate as well and
14 Debtor has no right to retain them.

15 The benefit of discharge is reserved for "the honest but
16 unfortunate debtor." In re Holstein, 299 B.R. 211, 233 (Bankr.
17 N.D. Ill. 2003). If section 727(d) is satisfied, the debtor has
18 been less than honest and deserves no discharge. In re Barr, 207
19 B.R. 160, 165 (Bankr. N.D. Ill. 1997).

20 To warrant revocation under section 727(d), the Trustee must
21 show that (1) such discharge was obtained through the fraud of the
22 debtor, and the requesting party did not know of such fraud until
23 after the granting of such discharge; (2) the debtor acquired
24 property that is property of the estate, or became entitled to
25 acquire property that would be property of the estate, and
26

1 knowingly and fraudulently failed to report the acquisition of or
2 entitlement to such property, or to deliver or surrender such
3 property to the trustee. 11 U.S.C. §727(d)(1)-(2).

4 Debtor failed to report the Chen Loan on his schedules when
5 his petition was filed and at no point did he amend his schedules
6 to reflect the debt. The evidence shows that the Trustee did not
7 learn of the Chen Loan until it was revealed in through discovery
8 in 2007. This was after the court discharged the Debtor. By
9 then, a substantial portion of the Chen Loan outstanding as of
10 Petition Date had already been paid to the Debtor. Debtor also
11 made no attempt to disclose the 2005 and 2007 Partnership
12 Distributions he received. These facts establish all the
13 necessary elements under both Sections 727(d)(1) and (2).

14 The Debtor possessed the necessary intent because he procured
15 his discharge by "fraud" or that he "knowingly and fraudulently"
16 failed to schedule the debt, report the payments or deliver the
17 monies to the Trustee. Section 727(d) does not require direct
18 evidence of intent.

19 The Debtor's fraudulent intent is clear from the fact that he
20 was aware of the omitted assets and knew his failure to list the
21 assets could seriously mislead the Trustee; in the alternative,
22 Debtor acted so recklessly in not reporting the asset that fraud
23 is implied.

24 Based on the behavior of the Debtor, his discharge should be
25 revoked pursuant to Section 727(d).
26

1
2 IV. CONCLUSION.

3 Trustee is entitled to a judgment on the second claim for
4 relief against Debtor in the amount of \$729,044.19 (for repayments
5 of the Chen Loan) and \$38,806.84 (for the Partnership
6 Distributions), plus costs. She is entitled to judgment against
7 Wong in the amount of at least \$11,000, plus costs.

8 At the time her counsel submits a form of judgment he may
9 also submit (without argument) a list of citations to the
10 appropriate exhibit number, page and entries where additional
11 payments on the Chen Loan to Wong have been documented. The list
12 should include a total dollar amount Trustee contends the judgment
13 against Wong should be. Counsel for Wong will then have ten days
14 to file a designation (also without argument) of any of the
15 Trustee's citations to the record he believes do not show a
16 payment to Wong on the Chen Loan. The court will determine
17 whether Trustee is entitled to a judgment against Wong in excess
18 of \$11,000.

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20 On the third claim for relief, Trustee is entitled to a
21 judgment revoking Chen's discharge.

22 Counsel for the Trustee should submit and serve in accordance
23 with B.L. R. 9021-1 a form of final judgment consistent with the
24 foregoing and for the reasons stated in this Memorandum Decision
25 (with the amount to be awarded against Wong left blank so the
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1 court may insert an amount) and consistent with the court's denial
2 of the motion to reconsider the grant of summary judgment in her
3 favor on the first claim for relief.

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5 * * * END OF MEMORANDUM DECISION * * *
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